

CHAPTER 225
RESALE AND PROCESSING EXEMPTIONS PRIMARILY
OF BENEFIT TO RETAILERS

Rules in this chapter include cross references to provisions in 701—Chapters 15, 17, 18 and 26 that were applicable prior to July 1, 2004.

701—225.1(423) Paper or plastic plates, cups, and dishes, paper napkins, wooden or plastic spoons and forks, and straws. When paper or plastic cups, plates, and dishes, paper napkins, and wooden or plastic spoons, forks, and other utensils are sold with food or other items to a buyer, and the buyer uses or consumes the utensils, sales of those utensils to retailers shall be considered sales for resale. The sales price from the sale of such items by retailers to consumers or users shall be subject to tax.

When these articles are transferred in connection with a service or sold for free distribution by retailers apart from a retail sale, the transaction shall be deemed to be a retail sale to the retailer and shall be taxable.

Sales of reusable placemats to retailers that sell meals shall be subject to tax.

EXAMPLE 1. A retailer purchases napkins and disposable forks and knives for the retailer's restaurant. The retailer provides these items free of charge, apart from the retail sale of food at the retailer's restaurant. Sale of these items to the retailer is a retail sale and is subject to tax.

EXAMPLE 2. A retailer purchases napkins and disposable forks and knives for the retailer's restaurant. The retailer sells these items with tangible personal property to the retailer's customers. The sale of these items to the retailer is considered a sale for resale and is not subject to Iowa sales tax at the time of purchase.

This rule is intended to implement Iowa Code section 423.3(2).

701—225.2(423) A service purchased for resale. A service is purchased for resale when it is subcontracted by the person who is contracted to perform the service.

225.2(1) *Services purchased for resale are purchased exempt from tax.*

EXAMPLE 1. X is a printer and enters into a contract with Y to print 500 bulletins. X subcontracts the job to Z. Z prints the 500 bulletins for X. There is no tax on the contracts between X and Z since X is purchasing the printing service from Z for resale to Y.

EXAMPLE 2. B owns a used car lot. E purchases an automobile from B. As a condition of such sale, B agrees to make repairs to the automobile. However, B subcontracts such repair work to C. E has agreed to pay B for the repair services and for the sale price of the automobile. Under these circumstances, the repair services furnished by C to B constitute a sale of such services to B for resale to E, who is the consumer of these services.

EXAMPLE 3. B owns an auto repair shop and C brings an automobile in to have the air conditioner fixed. B is unable to fix the air conditioner so the auto is sent to G, who is an air-conditioning specialist. The sale of G's service to B is a sale for resale by B to C.

225.2(2) *Services not purchased for resale.* The tax on services must be collected at the time the service is complete even if the service is not purchased by the ultimate beneficiary.

EXAMPLE. A operates a test laboratory business. A agrees to provide testing services to B. In the course of conducting the tests, A rents equipment from C. In computing the fee which B has agreed to pay A for testing services, A will include A's costs, including the rental A paid to C in rendering the testing services. Under these circumstances, A furnished B with testing services, and not with the equipment rental services which C furnished to A. A is the consumer of the equipment rental services which are not resold to B, and B is the consumer of the testing services.

This rule is intended to implement Iowa Code section 423.3(2).

701—225.3(423) Services used in the repair or reconditioning of certain tangible personal property. Services are exempt from tax when used in the reconditioning or repairing of tangible personal property of the type which is normally sold in the regular course of the retailer's business and which is held for sale by the retailer.

EXAMPLE 1. A owns a retail appliance store and contracts with B to repair a refrigerator that A is going to resell. A can purchase the repair service from B tax-free because A is regularly engaged in selling refrigerators and will offer the refrigerator for sale when it is repaired.

EXAMPLE 2. B, a used car dealer, owns a used car lot and contracts with C to repair a used car that B is going to sell. B can purchase the repair service from C tax-free because B is regularly engaged in selling used cars and will sell the used car after it is repaired.

EXAMPLE 3. C operates a retail farm implement dealership. C accepts a motorboat as part consideration for a piece of farm equipment. C then contracts with D to repair the motor on the boat. C does not normally sell motorboats in the regular course of C's business. Therefore, the service performed by D for C is subject to tax.

EXAMPLE 4. XYZ owns a retail radio and television store in Iowa and contracts with W to repair a television that XYZ is going to sell. XYZ can purchase television repair service tax-free from W because XYZ is regularly engaged in selling televisions subject to sales tax. However, in this instance XYZ sells the used television and delivers it into interstate commerce with the result that the Iowa sales tax is not collectible. Regardless of this fact, the exemption is applicable, and no Iowa tax is due for the television repair services performed.

This rule is intended to implement Iowa Code sections 423.1(50) and 423.1(51).

701—225.4(423) Tangible personal property purchased by a person engaged in the performance of a service.

225.4(1) In general.

a. Tangible personal property purchased by a person engaged in the performance of a service is purchased for resale and not subject to tax if (1) the provider and user of the service intend that a sale of the property will occur, and (2) the property is transferred to the user of the service in connection with the performance of the service in a form or quantity capable of a fixed or definite price value, and (3) the sale is evidenced by a separate charge for the identifiable piece or quantity of property.

b. Tangible personal property which is not sold in the manner set forth in "a" above is not purchased for resale and thus is subject to tax at the time of purchase by a person engaged in the performance of a service. Such tangible personal property is considered to be consumed by the purchaser who is engaged in the performance of a service, and the person performing the service shall pay tax upon the sale at the time of purchase.

EXAMPLE 1. An investment counselor purchases envelopes. These envelopes are used to send out monthly reports to the investment counselor's clients regarding their accounts. Tax is due at the time the investment counselor purchases the envelopes if the clients are not billed for these items. Each envelope is transferred to a client in a form or quantity which is capable of a fixed or definite price value. However, there must also be an actual sale to the client (customer) of an item of personal property in order that there be a "resale" of the item.

EXAMPLE 2. An automobile repair shop purchases solvents which are used in cleaning automobile parts and thus in performing its automobile repair service. Tax is due at the time the automobile repair shop purchases the solvents since the solvents are not sold to the customer and, in this case, the items are not transferred to a customer in a form or quantity which is capable of a fixed or definite price value. Thus, the solvents are deemed consumed by the purchaser engaged in the performance of the service.

EXAMPLE 3. A retailer purchases television picture tubes tax-free and makes a separate charge for the picture tube to the customer. Since the tube is transferred to the customer in a form or quantity capable of a fixed or definite price value, the retailer may purchase the picture tube exempt from tax for subsequent resale.

EXAMPLE 4. A beauty shop or barber shop purchases shampoo and other items to be used in the performance of its service. Tax is due at the time the beauty shop or barber shop purchases such items from its supplier because the customers of the beauty shop or barber shop are not separately billed for the items and because the items are not transferred to the customer in a form or quantity capable of a fixed or definite price value. The items are consumed by the beauty shop or barber shop.

EXAMPLE 5. A car wash purchases water, electricity, or gas used in the washing of a car. The car wash would be the consumer of the water, electricity, or gas, and tax is due at the time of purchase. The items purchased by the car wash are not transferred to the customer in a form or quantity capable of a fixed or definite price value, and the customer is not billed for the items.

EXAMPLE 6. An accounting firm purchases plastic binders which are used to cover the reports issued to its customers. These binders would be subject to tax at the time of purchase by the firm where the customer of the firm is not billed for the item, because there is no sale to the customer.

EXAMPLE 7. A meat locker purchases materials such as wrapping paper and tape which it uses to wrap meat for customers who provide the locker with the meat. These materials would be subject to tax at the time of purchase by the meat locker because they are not sold to the customer in a form or quantity capable of a fixed or definite price value.

EXAMPLE 8. A jeweler purchases materials such as main springs and crystals to be used in the performance of a service. These items are purchased by the jeweler for resale when they are transferred to the customer in a form or quantity capable of a fixed or definite price value, and each item is actually sold to the customer as evidenced by a separate charge therefor.

EXAMPLE 9. A lawn care service applies fertilizer, herbicides, and pesticides to its customers' lawns. The following are examples of invoices to customers which are suitable to indicate a lawn care service's purchase of the fertilizer, herbicides, and pesticides for resale to those customers: "Chemicals...31 Gal....\$60"; "Fertilizer...50 lbs....\$100"; and "Materials applied to lawn...4 bushel...\$40". The following are examples of information placed upon an invoice which would not indicate a purchase for resale to the customers invoiced: "Fifty percent of the charge for this service is for materials placed on a lawn," or "Lawn chemicals...\$30" or "Fifty pounds of fertilizer was applied to this lawn."

225.4(2) *Purchases made by automobile body shops or garages with body shops.* Tangible personal property purchased by body shops can be purchased for resale provided both of the following conditions are met:

a. The property purchased for resale is actually transferred to the body shop's customer by becoming an ingredient or component part of the repair work. See Iowa Code section 423.3(2).

b. The property purchased for resale is itemized as a separate item on the invoice to the body shop's customer and is transferred to the customer in a form or quantity capable of a fixed or definite price value.

If either of the above two conditions is not met, there is no purchase for resale and the body shop is deemed the consumer of the item purchased.

When body shops purchase items which will be resold (see list of items in this rule) in the course of the repair activity, the vendors selling to the body shops are encouraged to accept a valid resale certificate at the time of purchase. Reference rule 701—15.3(422,423). Failure of the vendor to accept a valid resale certificate may subject that vendor to sales tax liability since the burden of proof would be on the vendor that a sale was made for resale. If the vendor cannot meet that burden, the vendor will be liable for the sales tax. Such burden is not met merely by a showing that the purchaser had obtained from the department an Iowa retail sales tax permit or retail use tax permit.

For insurance purposes, body shops are reimbursed by insurance companies for “materials” which such shops consume in rendering repair services. Some of the materials are transferred to the recipients of the repair services and some are not. Of those so transferred, such transfer is in irregular quantities and is not in a form or quantity capable of a fixed or definite price value. Therefore, body shops are generally deemed to be the consumers of materials and must pay tax on these items at the time of purchase. Nonexclusive examples of items most likely to be included in this category of “materials,” whether actually transferred to customers of body shops or not, are as follows:

- Abrasives
- Battery water
- Body filler or putty
- Body lead
- Bolts, nuts and washers
- Brake fluid
- Buffing pads
- Chamois
- Cleaning compounds
- Degreasing compounds
- Floor dry
- Hydraulic jack oil
- Lubricants
- Masking tape
- Paint
- Polishes
- Rags
- Rivets and cotter pins
- Sanding discs
- Sandpaper
- Scuff pads
- Sealer and primer
- Sheet metal
- Solder
- Solvents
- Spark plug sand
- Striping tape
- Thinner
- Upholstery tacks
- Waxes
- White sidewall cleaner

The following are nonexclusive examples of parts which can be purchased for resale since they are generally transferred to the body shop’s customer during the course of the repair in a form or quantity capable of a fixed or definite price value and are generally itemized separately as parts.

- Accessories
- Batteries
- Brackets
- Bulbs
- Bumpers
- Cab corners
- Chassis parts
- Door guards

Door handles
Doors
Engine parts
Fenders
Floor mats
Grilles
Headlamps
Hoods
Hubcaps
Radiators
Rocker panels
Shock absorbers
Side molding
Spark plugs
Tires
Trim
Trunk lids
Wheels
Window glass
Windshield ribbon
Windshields

The following are nonexclusive examples of tools and supplies which are generally not transferred to the body shop's customer during the course of the repair and, therefore, could not be purchased for resale. The body shop is deemed the consumer of these items since they are not transferred to a customer. Therefore, the body shop must pay tax to the vendor at the time of purchase.

Air compressors and parts
Body frame straightening equipment
Brooms and mops
Buffers
Chisels
Drill bits
Drop cords
Equipment parts
Fire extinguisher fluids
Floor jacks
Hand soap
Hand tools
Office supplies
Paint brushes
Paint sprayers
Sanders
Signs
Spreaders for putty
Washing equipment and parts
Welding equipment and parts

Because of the nature of the body shop business and the formulas devised by the insurance industry to reimburse body shops for cost of “materials,” it is possible for body shops, in their invoices to their customers, to separately set forth labor, resold parts, and materials. While the materials can be separately invoiced as one general item, there is no way to ascertain a definite and fixed price for each item of the materials listed in this rule and consumed by the body shops, and some of such individual materials are not even transferred by body shops to their customers. Therefore, the body shops are generally the “consumers” of “materials” and do not purchase them for resale. See *W. J. Sandberg Co. v. Iowa State Board of Assessments and Review*, 225 Iowa 103, 278 N.W. 643 (1938). Thus, body shops should pay tax to their suppliers on all materials purchased and consumed by body shops. If materials are purchased from non-Iowa suppliers that do not collect Iowa tax from body shops, such body shops should remit consumer use tax to the department of revenue on such materials.

Body shops must collect sales tax on the taxable service of repairing motor vehicles. See rule 701—221.62(423). However, due to the nature of the insurance formulas, it is possible for body shops to itemize that portion of their billing which would be for repair services and that portion relating to consumed “materials.” It is also possible for body shops to itemize that portion of their charges for parts which they purchase for resale to their customers. Body shops do not and cannot resell the tools and supplies previously listed in this rule; their purchases of such items are taxable.

Therefore, as long as body shops separately itemize on their invoices to their customers the amounts for labor, parts, and for “materials,” body shops should collect sales tax on the labor and the parts, but not on the materials as enumerated in this rule.

EXAMPLE. A body shop repairs a motor vehicle by replacing a fender and painting the vehicle. In doing the repair work, the body shop uses rags, sealer and primer, paint, solder, thinner, bolts, nuts and washers, masking tape, sandpaper, waxes, buffing pads, chamois, and polishes. In its invoice to the customer, the labor is separately listed at \$600, the part (fender) is separately listed at \$600, and the category of “materials” is separately listed for a lump sum of \$200, for a total billing of \$1,400. The Iowa sales tax computed by the body shop should be on \$1,200, which is the amount attributable to the labor and the parts. The materials consumed by the body shop were separately listed and would not be included in the tax base for the taxable “sales price,” as defined in Iowa Code section 423.1(47), which is taxable under Iowa Code section 423.2.

In this example, if the “materials” were not separately listed on the invoice, but had been included in either or both of the labor or parts charges by marking up such charges, the body shop would have to collect sales tax on the full charges for parts or labor even though tax was paid on materials by the body shop to its supplier at the time of purchase.

This rule is intended to implement Iowa Code sections 423.1(35) and 423.3(2).

701—225.5(423) Maintenance or repair of fabric or clothing. Sales of chemicals, solvents, sorbents, or reagents directly used and consumed in the maintenance or repair of fabric or clothing are exempt from tax. See 701—Chapter 211 for definitions of the terms “chemical,” “solvent,” “sorbent,” and “reagent.” This rule’s exemption is mainly applicable to dry-cleaning and laundry establishments; however, it is also applicable to soap or any chemical or solvent used to clean carpeting. The department presumes that a substance is “directly used” in the maintenance or repair of fabric or clothing if the substance comes in contact with the fabric or clothing during the maintenance or repair process. Substances which do not come into direct contact with fabric or clothing may, under appropriate circumstances, be directly used in the maintenance or repair of the fabric or clothing, but direct use will not be presumed.

The following are examples of substances directly used and consumed in the maintenance or repair of fabric or clothing: perchloroethylene (also known as “perch”) or petroleum solvents used in dry-cleaning machines and coming in direct contact with the clothing being dry-cleaned. Substances used to clean or filter the “perch” or petroleum solvents would also be exempt from tax, even though these substances do not come in direct contact with the clothing being cleaned. The sale of soap or detergents especially made for mixing with “perch” or petroleum solvents is exempt from tax. The sale of stain removers to dry cleaners is exempt from tax.

A commercial laundry’s purchase of detergents, bleaches, and fabric softeners is exempt from tax. A commercial laundry’s purchase of water, which is a solvent, is also exempt from tax if purchased for use in the cleaning of clothing.

The purchase of starch by laundries and “sizing” by dry cleaners is not exempt from tax.

This rule is intended to implement Iowa Code section 423.3(50).

701—225.6(423) The sales price from the leasing of all tangible personal property subject to tax. See 701—Chapter 211 for the definitions of the words “lease or rental” and “tangible personal property” which are applicable to this rule.

225.6(1) *Past and present taxation of leases.* Prior to July 1, 2004, the rental of tangible personal property was treated as a taxable service for the purposes of Iowa sales and use tax law; reference 2003 Iowa Code section 422.43(11) and 701—subrule 26.18(2). The “rental” of tangible personal property was not a “sale” of that property, and therefore a purchase for subsequent leasing or rental was not a purchase for resale. See *Cedar Valley Leasing, Inc. v. Iowa Department of Revenue*, 274 N.W.2d 357 (Iowa 1979).

On and after July 1, 2004, the rental of tangible personal property is treated as the sale of that property for the purposes of Iowa sales and use tax law because “leases” and “rentals” of tangible personal property are taxable retail “sales” of that property. The rental of tangible personal property is no longer listed as a taxable enumerated service. The resale exemption in favor of sales for resale of tangible personal property is now applicable to sales and leases of tangible personal property for subsequent rental or lease.

EXAMPLE A. Al’s Rent All buys blowers, hand tools, ladders, plumbers’ snakes, sanders, and tillers for subsequent short-term rental to various customers. Al’s purchases of these items of equipment are purchases for resale and are exempt from tax as of July 1, 2004.

EXAMPLE B. In addition to its purchases of equipment for subsequent rental, Al’s Rent All leases from its suppliers, long-term, items of heavier equipment such as backhoes, forklifts, manlifts, tractors, and trenchers, again for subsequent leasing to various customers. Since the leasing of tangible personal property is now a purchase of that property, Al’s leasing for later sublease is a purchase of tangible personal property and is exempt from tax at the time of purchase as the purchase of tangible personal property for subsequent resale.

225.6(2) Distinguishing leases and rentals of tangible personal property from the furnishing of nontaxable services. In order to determine whether a particular fee is charged for the rental of tangible personal property or for the furnishing of a nontaxable service, the department looks at the substance, rather than the form, of the transaction. When the possession and use of tangible personal property by the recipient is merely incidental as compared to the nontaxable service performed, all of the sales price is derived from the furnishing of such nontaxable service and, unless a separate fee or charge is made for the possession and use of tangible personal property, no sales price is derived from the rental of tangible personal property. When the nontaxable service is merely incidental to the possession and use of the tangible personal property by the recipient, all of the sales price is derived from the furnishing of tangible personal property rental and, unless a separate fee or charge is made for the nontaxable service, no sales price is derived from the nontaxable service. When a tangible personal property rental agreement contains separate fee schedules for rent and for nontaxable service, only the sales price derived from the tangible personal property rental is subject to tax. This rule is not to be so construed as to be at variance with Iowa Code sections 423.2(8) and 423.3(70) concerning bundled service contracts and transportation services respectively.

225.6(3) Rental of real property distinguished from rental of tangible personal property. If a rental contract allows the renter exclusive possession or use of a defined area of real property and, incident to that contract, tangible personal property is provided which allows the renter to utilize the real property, if there is no separate charge for rental of tangible personal property, the sales price is for the rental of real property and is not subject to tax, unless taxable room rental is involved; reference rule 701—18.40(422,423).

If a person rents tangible personal property and, incidental to the rental of the property, space is provided for the property's use, the sales price from the rental shall be subject to tax. It may at times be difficult to determine whether a particular transaction involves the rental of real property with an incidental use of tangible personal property or the rental of tangible personal property with an incidental use of real property.

225.6(4) Rental of tangible personal property and rental of fixtures. The rental of tangible personal property which shall, prior to its use by the renter under the rental contract, become a fixture shall not be subject to tax. Such a rental is the rental of real property rather than tangible personal property. In general, any tangible personal property which is connected to real property in a way that it cannot be removed without damage to itself or to the real property is a fixture. See *Equitable Life Assurance Society of the United States v. Chapman*, 282 N.W. 355 (Iowa 1983) and *Marty v. Champlin Refining Co.*, 36 N.W.2d 360 (Iowa 1949). The rental of a mobile home or manufactured housing, not sufficiently attached to realty to constitute a fixture, is room rental rather than tangible personal property rental and subject to tax on that basis; see *Broadway Mobile Home Sales Corp. v. State Tax Commission*, 413 N.Y.S.2d 231 (N.Y. 1979). Reference also rule 701—18.40(422,423).

225.6(5) Rental of tangible personal property embodying intangible personal property rights—transactions taxable and exempt. Under the law, the sales price from rental of tangible personal property includes royalties and copyright and license fees. The rental of all property which is a tangible medium of expression for the intangible rights of royalties and copyright and license fees is subject to tax. Thus the sales price from the rental of films, videodiscs, videocassettes, and any computer software (other than rental of custom programs, reference 701—paragraph 18.34(3)“a”) which is the tangible means of expression of intangible property rights is subject to tax. The rental of such tangible property shall be subject to tax whether the property is held for rental to the general public or for rental to one or a few persons. See *Boswell v. Paramount Television Sales, Inc.*, 282 So.2d 892 (Ala. 1973). Reference also rule 701—17.18(422,423) regarding the exemption from the requirements of this sub-rule for rental of films, videotapes and other media to lessees imposing a taxable charge for viewing or rental of the media or to lessees that broadcast the contents of these media for public viewing or listening.

225.6(6) Deposits and additional fees. Taxability of a deposit required by an owner of rental property as a condition of the rental depends upon the type of deposit required. A deposit subject to forfeiture for the lessee's failure to comply with the rental agreement is not subject to tax. This type of deposit is separate from the rental payments and therefore is not taxable as part of the rental. Such deposits may include those for reservation, late return of the rental property or damage to the rental property. Deposits not subject to forfeiture which represent part of the rental receipts are considered part of the taxable rental and are subject to tax. Such deposits may include a deposit of the first rental payment which is applied to the rental receipts.

When tangible personal property is rented for a flat fee per month, per year, or for other designated periods, plus an additional fee based on quantity and capacity of production or use, the entire charge is taxable.

225.6(7) Leasing of tangible personal property moving in interstate commerce.

a. On and after July 1, 2004, in the case of a lease or rental that requires recurring periodic payments, the first periodic payment is taxed to Iowa if the property was delivered to the lessee in Iowa. Periodic payments made subsequent to the first payment may be taxed only by the state in which the property is primarily located for the period covered by the payment. The primary property location shall be as indicated by an address for the property provided by the lessee that is available to the lessor from its records maintained in the ordinary course of business, when use of this address does not constitute bad faith. The property location shall not be altered by intermittent use at different locations, such as use of business property that accompanies employees on business trips and service calls.

b. Where a nonresident lessor leases tangible personal property to a resident or nonresident lessee and the lessee uses the property in Iowa, the nonresident lessor has the responsibility of collecting Iowa use tax on the lease payments if Iowa is the primary location of the property, provided the lessor maintains a place of business in Iowa as described in 2005 Iowa Code sections 423.1(43) and 423.14(2). Whether the lease agreement is executed in Iowa or not is irrelevant. *State Tax Commission v. General Trading Co.*, 322 U.S. 335, 64 S.Ct. 1028, 88 L.Ed 1309 (1944).

c. Where a lessee is the recipient of equipment rental services sourced to Iowa and no tax has been collected from such lessee by the lessor, the lessee should remit Iowa use tax to the department of revenue. In the event no tax is remitted, the department, in its discretion, may seek to collect the tax from the lessor or lessee. In the event that the lessee rents tangible personal property, and the lessor does not maintain a place of business in Iowa and does not collect use tax pursuant to 2005 Iowa Code section 423.14, such lessee shall remit tax on its rental payments to the department.

d. Where a resident lessor leases equipment to a nonresident lessee outside Iowa and the equipment is delivered to the lessee outside Iowa, the act of leasing is exempt from the Iowa sales tax on the rental payments. However, in the event the lessee brings the equipment into Iowa, uses it in Iowa, and Iowa becomes the primary location of the property, Iowa use tax applies to subsequent rental payments.

e. If a sales or use tax has already been paid to another state on the sales price of tangible personal property prior to the use of that property in Iowa, a tax credit against the Iowa use tax on the purchase price will be given. After the equipment is brought into Iowa, if a sales or use tax is properly payable and is paid to another state on the rental payments of equipment, for the same time the Iowa tax is imposed on such rentals, a tax credit against the Iowa use tax on such rental payments will be given.

This rule is intended to implement Iowa Code sections 423.1(22), 423.1(43), 423.1(45), 423.1(54), 423.2(1), and 423.15(2).

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